The Pension Digest

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ALSO IN THIS ISSUE –

Collin W. Fritz and Associates, Inc.,
"The Pension Specialists"

U.S. Government Enters the Roth IRA Business With myRA!

The Obama administration has done many things to expand the role of the federal government in the lives of ordinary Americans, but it has recently taken a giant step forward so that the federal government can take a more active role with respect to retirement savings and investments.

The United States is going into the IRA business, more specifically the Roth IRA business. myRA is a Roth IRA, nothing more and nothing less. The Treasury Department does not make this fact as clear or as transparent as it should. There is no discussion that the maximum contribution amount for a person younger than age 50 is $5,500, for a person age 50 or older is $6,500 and that these limits are reduced by other IRA contributions. There is no discussion of the fact that an individual's maximum contribution amount is reduced when his or her MAGI is in the range of $114,000-$129,000 and $181,000 to $191,000. There is no discussion that a person must have compensation in order to make a contribution to a myRA just as if he or she must have when making a contribution to a Roth IRA.

Rather than investing a person's Roth IRA contributions in a time deposit, certificate of deposit, or savings accounts as offered by an FDIC insured financial institution or other non-insured investments as offered by investment firms, the

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Warning: U.S. Tax Court Rejects IRS Policy on the One Rollover Per 12-Month Rule

Commencing immediately, an IRA custodian/trustee will need to start applying a new rule for when it is receiving an IRA rollover contribution.

Since at least 1989 the IRS has stated in Publication 590 that the once per year rollover rule applies on a per IRA plan agreement basis and not to all of a person's IRAs. That is, if two distribution are taken from the same IRA, then only one of them could be rolled over. A distribution taken from a different IRA could be rolled over even though a person had taken a distribution from another IRA and rolled it over within the 12-month period. The 2013 version states the following on page 25.

> **Waiting period between rollovers.** Generally, if you make a tax-free rollover of any part of a distribution from a traditional IRA, you cannot, within a 1-year period, make a tax-free rollover of any later distribution from that same IRA. You also cannot make a tax-free rollover of any amount distributed, within the same 1-year period, from the IRA into which you made the tax-free rollover.
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> The 1-year period begins on the date you receive the IRA distribution, not on the date you roll it over into an IRA.
>
> ***Example.*** You have two traditional IRAs, IRA-1 and IRA-2. You make a tax-free rollover of a distribution from IRA-1 into a new traditional IRA (IRA-3). You cannot, within 1 year of the distribution from IRA-1, make a tax-free rollover of any distribution from either IRA-1 or IRA-3 into another traditional IRA.
>
> However, the rollover from IRA-1 into IRA-3 does not prevent you from making a tax-free rollover from IRA-2 into any other traditional IRA. This is because you have not, within the last year, rolled over, tax free, any distribution from IRA-2 or made a tax-free rollover into IRA-2.

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myRA contributions will be invested in a special investment or deposit account that "will earn interest at the same variable rate as the Government Securities Investment Fund in the Thrift Savings Plan for federal employees." myRA's will be backed by the full faith and credit of the United States.

The U.S. Department of the Treasury will either administer the myRA Program itself or hire a financial institution to serve as the Roth IRA custodian/trustee and administer these accounts. Under current law, the governing IRA regulation does not authorize the U.S. government to serve as an IRA custodian/trustee. Late 2014 is the tentative goal of the Treasury to implement the myRA program. Most likely this program will not be implemented until after the November 2014 elections. Many new forms will need to be written for the myRA and computer software will need to be developed and tested.

The main features of the myRA program are:

1. Small contributions may be made. An initial contribution of $25 is required and subsequent contributions would need to be $5.
2. No administrative fees would be charged – opening, closing, transferring, distributions, investing, etc. A guarantee is given that there may be no investment loss.
3. myRA is initially to be a payroll deduction program. That is, the individual cannot make his or her contributions via the web. Rather, the individual's employer must withdraw the contribution amount from each individual's payroll and that day the employer will send a direct deposit to each participating employee's myRA. The employer's role is limited to providing information to its employees as to how the myRA program works, having the employee complete a form as to how much is to be withheld and then transmitting such myRA contributions. An individual would sign-up online.
4. Distributions may be taken at any time. It will be interesting to see if a person will be able to withdraw funds online. Rollovers will also be permitted. Additional guidance will need to be furnished by the IRS. An individual will be able to voluntarily rollover his or her myRA to another eligible retirement. Under current law, the only plan to which Roth IRA funds may be rolled over to is another Roth IRA. Presumably, the only plan to which myRA funds may be rolled over to is Roth IRA. Once the balance in the myRA reaches $15,000 or after 30 years, the balance in the myRA must be rolled over to a Roth IRA as authorized by current law. The Treasury Department seems to give the impression that there might be other private sector retirement accounts which could accept such a rollover. There is no discussion of transferring funds from a myRA to a Roth IRA.

What is the Obama administration and the current Treasury Department leaders trying to accomplish by creating this myRA program?

The Obama administration does want more individuals to save for retirement.This is an important public purpose. The reality is, however, too many individuals are not making the IRA contributions one would expect or hope would be made. Not everyone participates in a 401(k) plan. Due to the complexity of the federal tax laws applying to pension plans, many small employers don't sponsor pension plans for their employees. Once the economy improves, it may be that such employees would make IRA contributions.

The myRA program is a trial program. It may be an unspoken trial program, but that is what it is. Many in the Obama administration would like to see the U.S. government do much more than is presently being done to assure the majority of low and moderate income individuals will have retirement funds in addition to Social Security.

After seeing how the myRA program works or doesn't work, the Obama administration may try to seek to have all employers, even small employers, sponsor and make contributions to federally run profit sharing/pension plans or federally run employees' IRAs. That is contributions by employers become mandatory rather than voluntary as under existing law. And the government makes the investments rather than the individuals as too many individuals tend to make poor investments.

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Time will tell if sufficient employers will voluntarily participate in the myRA program to make it a success. We have doubts. Certainly the goal to increase retirement savings is worthwhile, but a simpler approach has a better chance of accomplishing this. The simplest approach is that the individual makes a contribution into his or her own IRA without involving the employer.

It Was Mandatory to Furnish FMV IRA Statements by January 31, 2014

This article is being written since it appears that some financial institutions did not furnish an IRA FMV statement by January 31, 2014. They did furnish the 1099-R forms and RMD notices, but not the FMV statements. These institutions have come to believe that it is no longer necessary to furnish a separate FMV statement in January because this information is furnished when the 2013 Form 5498 is furnished in May. Actually, June 2 since May 31 is a Saturday this year. Some institutions believe this because that is what their large data processor is telling them.

Both the institution and the data processor may learn an IRS reporting lesson the hard way. The IRS may assess a fine of $50 per IRA for each FMV statement furnished late or not at all. For example, if an institution failed to furnish its 800 IRA accountholders the FMV statement by January 31, 2014, then the IRS may assess a fine of $40,000.

The IRS will look to collect the penalty from your institution and you will need to find out if the data processor will agree to pay some or all of the penalty. Hopefully, individuals and tax preparers do not report an institution to the IRS for failing to furnish the FMV statement by January 31, 2014.

If your financial institution did not mail the FMV statements to your IRA accountholders and inheriting beneficiaries by January 31, 2014, you want to do so as soon as possible in order to limit the potential fine.

The IRS instructions for completing the 2013 Form 1099-R and Form 5498 also set forth the rules for furnishing the 2013 FMV statements and the 2014 RMD notices. See the highlighted portions of pages 20 and 21. The rule is, "By January 31, 2014, you (the custodian) must provide participants with a statement of the December 31, 2013, value of the participant's account, and RMD, if applicable."

There is a separate and distinct rule for furnishing the 2013 Form 5498. You (the custodian) must furnish the Form 5498 to the participant and file a copy with the IRS by June 2, 2014.

The fact that the Form 5498 is furnished between April 16 and June 2 does not relieve the IRA custodian of furnishing the FMV statement by January 31, 2014.

Why must the IRA custodian furnish the statement by January 31, 2014?

The IRS has a good tax reason. The problem is, the IRS has never furnished an easy to understand explanation. If an individual must file Form 8606 (Nondeductible IRAs), he or she (or the accountant) must use the FMV statement (s) to prepare Section I of the Form 8606. Remember, that a person who has multiple IRAs, including traditional, SEP and SIMPLE, must aggregate the information from all such IRAs for various contribution and distribution purposes. It does not matter that most IRA accountholders have never made a nondeductible contribution. Such information may also be important for certain Roth IRA distributions.

A financial institution must furnish all required IRS reporting forms. Sometimes a data processor may think it is doing the financial institution a favor and it is saving the institution money by not preparing a certain form or statement. That will be the case only if the data processor understands the applicable IRS rules for IRAs. The financial institution wants to make sure that when a data processor informs you that furnishing a form or statement is no longer required that the data processor is correct. Some times the data processor is incorrect.

In the March or April newsletter, we will again discuss the options available so that an IRA custodian will comply with the FMV statement requirements. Not furnishing the FMV statement by January 31 is not one of the options.

A Special Law Allows Larger Contributions for 1-Person 401(k) Plans – $56,500 vs $51,000

We all know the federal income tax law are too complicated and need to be simplified. It would also help if the IRS (and sometimes CWF) would do a better job of explaining these tax laws.

Set forth below is an IRS table or chart comparing various contribution rules for SEPs, SIMPLEs, 401(k) and non-40l(k) qualified plans and defined benefit pension plans. This chart comes from the introductory section of Publication 560 (Retirement Plans for Small Business). Note that there is no explanation near the chart that the $51,000 is increased to be $56,500 if an individual is age 50 or older and is a participant of a 401 (k) plan.

Why is the maximum limit for 2013 increased to $56,500 for 401(k) participants age 50 or older?

The term catch-up contribution is now quite common with respect to IRA and pension contributions. IRA accountholders who age 50 or older can make an additional catch-up contribution of $1,000. An HSA owner age 55 or older can make a catch-up contribution of $1,000. A 401(k) participant age 50 or older is allowed to make an additional elective deferral contribution of $5,500.

A tax law enacted in 2001, Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) authorized an individual age 50 or older to make additional elective deferral contributions each year, up to a certain limit if the plan was written to authorize such additional elective deferral contributions. Such contributions are now called catch-up contributions and these catch-up contributions are NOT subject to various limits that apply to the individual and the employer. For example, the maximum amount which an employer can contribute on behalf of a participant is $51,000 for 2013. The catch-up amount of $5,500 does not count against this limit; the $5,500 is in addition to this limit. And any catchup elective deferral contributions are not subject to the ADP/ACP nondiscrimination tests.

Note that this additional $5,500 applies only to 401(k) plans, it does not apply to SEP plans and profit sharing plans with no 401 (k) feature.

Table 1. Key Retirement Plan Rules for 2013

Type of Plan	Last Date for Contribution	Maximum Contribution	Maximum Deduction	When To Set Up Plan
SEP	Due date of employer's return (including extensions).	Smaller of $51,000 or 25%[1] of participant's compensation.[2]	25%[1] of all participants' compensation.[2]	Any time up to the due date of employer's return (including extensions).
SIMPLE IRA and SIMPLE 401(k)	**Salary reduction contributions:** 30 days after the end of the month for which the contributions are to be made.[4] **Matching or nonelective contributions:** Due date of employer's return (including extensions).	**Employee contribution:** Salary reduction contribution up to $12,000, $14,500 if age 50 or over. **Employer contribution:** *Either* dollar-for-dollar matching contributions, up to 3% of employee's compensation,[3] *or* fixed nonelective contributions of 2% of compensation.[2]	Same as maximum contribution.	Any time between 1/1 and 10/1 of the calendar year. For a new employer coming into existence after 10/1, as soon as administratively feasible.
Qualified Plan: Defined Contribution Plan	**Elective deferral:** Due date of employer's return (including extensions).[4] **Employer contribution:** Money Purchase or Profit-Sharing: Due date of employer's return (including extensions).	**Employee contribution:** Elective deferral up to $17,500, $23,000 if age 50 or over. **Employer contribution:** Money Purchase: Smaller of $51,000 or 100%[1] of participant's compensation.[2] Profit-Sharing: Smaller of $51,000 or 100%[1] of participant's compensation.[2]	25%[1] of all participants' compensation[2], plus amount of elective deferrals made.	By the end of the tax year.
Qualified Plan: Defined Benefit Plan	Contributions generally must be paid in quarterly installments, due 15 days after the end of each quarter. See *Minimum Funding Requirement* in chapter 4.	Amount needed to provide an annual benefit no larger than the smaller of $205,000 or 100% of the participant's average compensation for his or her highest 3 consecutive calendar years.	Based on actuarial assumptions and computations.	By the end of the tax year.

[1]Net earnings from self-employment must take the contribution into account. See Deduction Limit for Self-Employed Individuals in chapters 2 and 4 .
[2]Compensation is generally limited to $255,000 in 2013.
[3]Under a SIMPLE 401(k) plan, compensation is generally limited to $255,000 in 2013.
[4]Certain plans subject to Department of Labor rules may have an earlier due date for salary reduction contributions and elective deferrals.

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Warning: U.S. Tax Court Rejects IRS Policy on the One Rollover Per 12-Month Rule,
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A recent U.S. Tax Court case is a classic illustration that there are times the IRS wants to collect taxes so strongly from a particular taxpayer that the IRS personnel in charge is willing to have the decision cause the general public large tax administrative problems. Such is the result of a recent U.S. Tax Court case, A.L. Brobrow and E.S. Brobrow v. Internal Revenue Commissioner, T.C. Memo 2014-21 as decided on January 28, 2014.

The court expressly holds that the one year restriction between rollovers applies to all distributions from all IRAs and is not limited to the same IRA. The court found the applicable statue expressly authorizes just one rollover during the 12 month period commencing on the date of distribution when such distribution is rollover. The court did not discuss the subject if the IRS had the authority to modify this provision. The court wrote,

> Section 408(d)(3)(B) limits a taxpayer from performing more than one nontaxable rollover in a one-year period with regard to IRS and individual retirement annuities. Specifically, section 408(d)(3)(B) provides:
>
> This paragraph [regarding tax-free rollovers] does not apply to any amount described in subparagraph (A)(i) received by an individual from an individual retirement account or individual retirement annuity if at any time during the 1-year period ending on the day of such receipt such individual received any other amount described in that subparagraph from an individual retirement account or an individual retirement annuity which was not includible in his gross income,because of the application of this paragraph.
>
> The reference to "any amount described in subparagraph (A)(i)" refers to any amount characterized as a nontaxable rollover contribution by virtue of that amount's being repaid into a qualified plan within 60 days of distribution from [*9] IRA or individual retirement annuity. <u>The one-year limitation period begins on the date on which a taxpayer withdraws funds from an IRA or individual retirement annuity and has no relation to the calendar year.</u>
>
> The plain language of section 408(d)(3)(B) limits the frequency with which a taxpayer may elect to make a nontaxable rollover contribution. By its terms, the one-year limitation laid out in section 408(d)(3)(B) is not specific to any single IRA maintained by an individual but instead applies to all IRAs maintained by a taxpayer. Section 408(d)(3)(B) speaks in general terms: An individual may not receive a nontaxable rollover from "<u>an</u> individual retirement account or individual retirement annuity" if that individual has already received a tax-free rollover within the past year from "<u>an</u> individual retirement account or individual retirement annuity." (Emphasis added.)<u> In other words, a taxpayer who maintains [*13] multiple IRAs may not make a rollover contribution from each IRA within one year.</u>

What were the facts of this case?

Mr. Brobrow maintained two traditional IRAs at Fidelity Investments. One was a rollover IRA. His wife maintained her own traditional IRA. The couple must have had cash flow problems. Fidelity's advisers apparently told him he could to do the following.

Step 1. On April 14, 2008, he withdrew $65,064 from his IRA #l. He did take two distributions. It may be he needed these funds to pay tax liabilities which had to be paid by the April 15th.

Step #2. On June 6, 2008, he withdrew $65,064 from his IRA #2.

Step #3. On June 10, 2008, he made a rollover contribution of $65,064 into IRA #l. The funds had come from his personal checking or investment account.

Step #4. On July 31, 2008, she withdrew $65,064 from her personal traditional IRA. These funds were deposited into a joint account.

Step #5. On August 4, 2008, Mrs. Brobrow made a rollover contribution of $65,064 into his IRA #2. The funds for this rollover came from their joint account.

Step #6. On September 30, 2008, she made a rollover contribution of $40,000 into her traditional IRA. The funds came from their joint account. Note her withdrawal of $65,064, however, was taxable as she made her rollover contribution on day 61 and not on day 60.

If the court had followed the IRS statement set forth in the 2007 or the 2008 Publication 590, Mr. Brobrow's two withdrawals of $65,064 would not have been taxable. He rolled over both within the 60 day time period. He had not rolled over a previous distribution from the two IRAs within the preceding 12 months.

Actions by an IRA Custodian/Trustee.

CWF is in the process of revising its rollover certification forms to state the 12 month rule is no long one per plan agreement. The Disclosure Statement of the IRA Plan Agreement booklet will also be revised. An IRA custodian/trustee will want to send an amendment to its IRA accountholders informing them of this change. It must be remembered that any distribution after the one which is rolled over is now taxable. One way to inform the existing accountholders would to to furnish the 2013-2014 Comprehensive IRA Amendment which discusses this change. CWF should have the revised forms ready by March 7.

Reminder: No Requirement to Withdraw Earnings When Excess is Withdrawn After the Due Date (April 15 or October 15)

There are current year excess contributions and there are "older" excess contributions. When an individual withdraws a current year excess contribution, there is a requirement to withdraw the related income. When an individual withdraws an "older" excess contribution, he or she is not required to withdraw any related income. A fair number of tax preparers and IRA representatives believe there is always a requirement to take out the earnings when an individual is withdrawing an excess contribution. There is no such requirement if the excess is an "older" excess contribution.

For example, Mary Customer made a $5,000 contribution to her Roth IRA on April 10, 2012 for tax year 2011. She had previously made contributions to her Roth IRA for 4 years. For some reason, her tax accountant did not realize her 2011 income (MAGI) exceeded the Roth IRA contribution limit for 2011 and therefore her $5,000 contribution was an excess contribution. Mary was also ineligible to make a 2012 Roth IRA contribution because her income was to high. On December 17, 2013 her accountant informs her of the error and that she should go into the Roth IRA custodian and withdraw the $5,000 and the earnings. There is no need to withdraw the earnings. The tax rules do not require it. The 2011 excess contribution is an "old" excess contribution. The deadline to correct this excess contribution without owing the 6% excess contribution tax was October 15, 2012. Since this deadline was not met, she owes the 6% excise tax on the $5,000 or $300 for 2011. She also the 6% excise tax on the $5,000 or $300 for 2012. Because she withdraws the $5,000 before December 31, 2013, she does not owe the 6% tax for 2013.

The approach of the law is - if an individual in this situation is required to pay penalty taxes for two years of $300 each or $600, she is not required to take out the related income. If she does take out the income, she will only be causing herself more tax difficulties as she is not required to take out the related income. And if she does withdraw an amount equal to the income, it will treated and reported as a nonexcess withdrawal.

Joint Revocable Trusts and IRAs May be a Tax Trap For the Unknowing

Jane and Mark are both age 63. In 2012 their attorney had written a joint revocable trust for them. Upon the death of the second spouse, the trust becomes irrevocable.

Both Jane and Mark have had their own traditional IRAs since 1983. Before this trust had been written, each had designated the other as his/her sole primary IRA beneficiary. In 2012 each had come into the IRA custodian and had changed the designated beneficiary of their IRA to be the joint revocable trust.

Jane died on February 10, 2013. Jane's IRA had a balance of $78,000 on February 10, 2013. Mark's IRA had a balance of $46,000.

Is there a tax trap? Yes. The beneficiary of Jane's IRA is no longer Mark, her spouse, rather it is the joint revocable trust. The beneficiary RMD rules require the five year rule to be used when the designated beneficiary is not a living person and she dies before required beginning date. This means the $78,000 must be distributed to the trust by December 31, 2018. This is a tax trap. Mark is no longer the beneficiary of her IRA. He may be a beneficiary of the revocable trust, but he is no longer the IRA beneficiary and he does not have the right to elect to treat her IRA as his own. Nor, does he have the right to take a distribution and then rollover such funds into his own traditional IRA.

A qualified trust for beneficiary RMD rule purposes is allowed to use the life distribution rule and the distributions may be paid out to the qualified trust using the age (life expectancy) of the oldest beneficiary of such trust as long as all beneficiaries are living individuals. However, one the rules which must be met to have a qualified trust is that the trust must be irrevocable after the IRA accountholder has died. Since Mark is still alive, the joint trust is not a qualified trust as it is still revocable.

It is okay for a married couple to establish a joint revocable trust, but what they don't want to do is designate this trust as the beneficiary of their respective IRAs. It is best that an individual designates directly his or her spouse A tax trap will catch a married couple with a joint revocable trust if they each designate the trust to be the beneficiary of their IRAs.

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Likely Prohibited Transaction Arising From the State of Minnesota's Angel Tax Program

The following letter was written to a financial institution acting as the IRA trustee of an individual's self-directed trust IRA. The individual had instructed to have some of her traditional IRA funds invested in a small Minnesota corporation. The investment was eligible for a special tax credit under Minnesota law. As will be discussed, if the credit is paid to her as the investor and not to her IRA, there will be prohibited transaction concerns. For discussion purposes her name is Clara Jones. Clara is married and she and her husband filed a married filing jointly Minnesota income tax return. Clara had transferred her IRA to Financial Institution ABC in June of 2013.

Here is CWF's letter to the IRA trustee

Dear Trustee:

You had called to discuss a tax refund check one of your clients had received. The check was actually issued by the Minnesota Management and Budget Division of the State of Minnesota. This check is related to a special tax credit authorized by the state of Minnesota for certain start-up investments. This credit is commonly called the Angel Investment Tax Credit. The actual name is the small business investment tax credit.

This check was made jointly payable to D. and C. Jones. A decision needs to be made regarding this check.

For the reasons discussed below, there are prohibited transaction concerns. Claiming the Minnesota Angel Tax Credit with respect to an IRA investment may well be a federal tax trap if IRA funds are used to make the investment. The IRS will be able to argue that a prohibited transaction will occur under Code section 4975.

In reviewing the tax and legal rules for the Angel Tax Credit program it is clear that the law grants the credit to an individual and there is no discussion of what is the result if a person self-directs IRA and/or pension funds to make the investment. The credit is a refundable credit and it is claimed on the Form M-1 and Form M1B.

The main concern is, the State of Minnesota issued the check to D. and Clara Jones since they had filed a joint tax return. The check was received. Code section 4975 (c) (1) sets forth 6 categories of acts which are prohibited transactions.

Subsection (D) provides that a "transfer to, or use by or for the benefit of, a disqualified person of the income or assets of a plan" is a prohibited transaction by her. The fact the tax instructions suggest she may contribute the check to her IRA does not resolve the problem.

Subsection (F) provides that the "receipt of any consideration for his own personal account by any disqualified person who is a fiduciary from any party dealing with the plan in connection with a transaction involving the income or assets of the plan" is also a prohibited transaction. She has received consideration. I don't believe that her agreeing to put the money into the IRA resolves the problem. Prohibited transaction situations/questions are complex. The federal tax consequences are extremely harsh. A prohibited transaction may occur with respect to an IRA transaction and a person may simply not think that a prohibited transaction might occur. I believe filing for this investment credit is such a situation. The Minnesota law has been written poorly. It should have been contemplated that many individuals would want to have such securities owned within their IRAs. In such case, the credit or rebate for making the desired investment would be returned directly to the IRA. Minnesota law does not do this. It requires that the check be made payable to the person.

D. and Clara Jones and their advisors must make their own decisions. Code section 4975 sets forth the prohibited transaction rules. These rules are jointly administered by the Department of Labor (DOL) and the IRS. When a prohibited transaction occurs, the federal tax law is - the IRA is deemed distributed as of the first day of a tax year. The individual must include the taxable portion is his income, the 10% additional tax is owed if the individual is under age 59 1/2, and the 20% underpayment tax will also likely be owed if not reported on their tax return.

As a general rule, an IRA trustee is able to follow the instructions of its client and tax advisors as long as there is a reasonable basis for their written tax position.

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The IRA trustee needs to be aware that it has certain IRA reporting duties as an IRA custodian/trustee. It is arguable as to how well-defined the reporting rules are. The IRS position is, if a prohibited transaction occurs, then the IRA trustee must use the reporting code "5" in box 7 on the Form 1099-R to report to both the individual and the IRS that a prohibited transaction has occurred. The penalty for not preparing a required Form 1099-R is $100.

Unlike with pension plans, the IRS at this time has no formal procedure for correcting IRA errors. The IRS has no formal procedure for allowing a prohibited transaction to be corrected by paying an amount less than the taxes to be assessed. Consideration should be given to discussing this situation with the DOL as the DOL has the primary authority for granting exemptions. That is, a prohibit transactions has or will occur, and the DOL will allow it (i.e. exempt it) as long as certain conditions are met.

I would like to think that the DOL would be willing to help in this situation by granting a retroactive exemption. The DOL does NOT have a filing fee. In prior years the DOL tended to not want to look at requests for IRA exemptions. The DOL has recently given the impression that they want to start handling more IRA situations. This situation may give them that opportunity.

What to do with the check if a PT exemption is not requested and /or received from the DOL?

Putting the funds in the IRA is better than just cashing the check on a personal basis. There is an attempt to correct the situation even though the IRS has no program allowing such a correction.

Another alternative to voluntarily correct the situation would be to withdraw their claim for the credit and return the check. An argument then could be made that there was no prohibited transaction.

The bank will need to consider what IRS reporting, if any, it would be required to do. The options - no reporting, prepare a Form 1099-R as he had receipt of the funds and then show the contribution as a rollover, or report on the Form 1099-R that a prohibited transaction has occurred.

Until Minnesota law is changed to allow an IRA to be a qualified investor rather than being limited to an individual and to allow the credit to be paid to the IRA, an individual does NOT want his or her IRA to purchase stock which qualifies for the special investment credit and then file to receive such credit.

No Withholding on CESA or HSA Distributions

There will be times when a good customer will request withholding of federal income tax with respect to a HSA distribution or a CESA distribution. You must instruct your personnel to politely inform your customer that the bank is unable to accommodate the request.

Federal tax law does not require a financial institution to withhold federal income tax with respect to an HSA or CESA distribution. An institution which withholds, when the law does not require it., may find it has a situation more complicated than it wants.

The IRS does not have any reporting procedures to accommodate a person who wants withholding with respect to an HSA withdrawal or an CESA withdrawal. There is no way for a financial institution to report or show the withholding amount on either the individual's Form 1099-Q (Payments From Qualified Education Programs Under Sections 529 and 530) or the Form 1099-SA (Distributions From an HSA). A financial institution is required to file Form 945 (Annual Return of Withheld Federal Income Tax) when it has withheld federal income. The instructions mention distributions from pensions, IRAs, 403(b) plans, 457(b) plans, annuities, military retirement pay, Indian gaming profits, gambling winnings, and any voluntary amount withheld on certain government payments. There is no mention of HSA or CESA distribution.

An institution will want to correct the situation if its personnel withholds federal income tax from such distribution. The institution will somehow need to get the money back from the IRS so it may pay the individual the withheld amount. This amount should have been paid to the individual. Most likely, the institution would off-set this amount which should not have been sent to the IRS with other funds which were withheld for other customers.